U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
ENTERED
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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

In re:	§	
	§	
MEDICAL SELECT MANAGEMENT,	§	CASE NO. 01-45298-BJH-11
	§	(CHAPTER 11)
Debtor.	§	

FINDINGS OF FACT AND CONCLUSIONS OF LAW IN SUPPORT OF CONFIRMATION OF TRUSTEE'S AND OFFICIAL UNSECURED CREDITORS' COMMITTEE'S FIRST AMENDED JOINT LIQUIDATING PLAN, AS MODIFIED, UNDER CHAPTER 11 OF THE UNITED STATES BANKRUPTCY CODE

On April 21 and May 5, 2004, the Court conducted a hearing (the "Confirmation Hearing") to consider confirmation of the Trustee's and Official Unsecured Creditors' Committee's First Amended Joint Liquidating Plan Under Chapter 11 of the United States Bankruptcy Code (the "Plan"), filed by Dennis S. Faulkner, the duly-appointed Chapter 11 Trustee in this case (the "Trustee"), and the Official Unsecured Creditors' Committee (the "Committee," and together with the Trustee, the "Proponents"). Having considered the Plan, all timely-filed objections to confirmation of the Plan, the Proponents' and other parties' respective replies to such objections, the pre-trial briefs of the parties, the evidence presented (including the proffered testimony of Dennis S. Faulkner and Randy Jones which was accepted without objection [*see* Proponents' Exhs. 22 & 28]), and argument of counsel, and the Proponents having made certain non-material modifications to the Plan and filed the Trustee's and Official Unsecured Creditors' Committee's First Amended Joint Liquidating Plan, as Modified, Under Chapter 11 of the United States Bankruptcy Code (the "Modified Plan"), the Court hereby enters its findings of fact and conclusions of law in support of confirmation of the Modified Plan, as follows:[1]

FINDINGS OF FACT

A. Procedural Background

1. On July 24, 2001 (the "Petition Date"), Medical Select Management f/k/a Harris Methodist Select (the "Debtor") filed its voluntary petition for relief under Chapter 11 of Title 11 of the United States Code, 11 U.S.C. § 101, *et seq.* (the "Bankruptcy Code"), thereby initiating the above-captioned and referenced case (the "Bankruptcy Case").

2. On or about August 15, 2001, the United States Trustee appointed the Committee in the Bankruptcy Case. The Committee is comprised of seven (7) unsecured creditors (or their representatives) in the Bankruptcy Case, five (5) of which are medical providers, and two (2) of which are health maintenance organizations (HMOs). The two HMO members are PacifiCare of Texas, Inc. ("PacifiCare") and Aetna Health Inc., as the successor in interest to Aetna U.S. Healthcare of North Texas Inc. ("Aetna," and together with PacifiCare, the "Settling HMOs"). During the course of the Bankruptcy Case, the Committee established a sub-committee, comprised of each of the members of the Committee with the exception of the Settling HMOs, for the purpose of analyzing issues related to, and negotiating with, the Settling HMOs. Accordingly, any mention of the Committee herein is in reference to such sub-committee.

3. On September 24, 2001, the Court ordered the appointment of a Chapter 11 trustee in the Bankruptcy Case. In accordance therewith, the United States Trustee appointed the

[1] Each finding of fact set forth herein, to the extent it is or may be construed as a conclusion of law, shall also constitute a conclusion of law. Each conclusion of law set forth herein, to the extent it is or may be construed as a finding of fact, shall also constitute a finding of fact. Additionally, capitalized terms herein shall have the meanings assigned to them in the Modified Plan unless otherwise separately defined herein.

Trustee to serve as the Chapter 11 trustee. By order entered on October 11, 2001, the Court confirmed and approved the Trustee's appointment.

4. On December 30, 2003, the Proponents filed the Plan. *See* Proponents' Exh. 2. On January 28, 2004, the Proponents filed their Second Amended Joint Disclosure Statement Pursuant to 11 U.S.C. § 1125 in Support of Trustee's and Official Unsecured Creditors' Committee's First Amended Joint Liquidating Plan Under Chapter 11 of the United States Bankruptcy Code (the "Disclosure Statement"). *See* Proponents' Exh. 1.

5. On or about January 29, 2004, the Court entered an Order (A) Approving the Proponents' Second Amended Joint Disclosure Statement, (B) Scheduling Hearing to Consider Confirmation of Proponents' First Amended Joint Liquidating Plan, (C) Establishing Voting and Objection Deadlines on Plan, (D) Approving Forms of Ballots and Solicitation Procedures, and (E) Approving Form and Manner of Notice (the "Disclosure Statement Order"). *See* Proponents' Exh. 3. Pursuant to the Disclosure Statement Order, the Court approved the Disclosure Statement as containing "adequate information" as required by Section 1125 of the Bankruptcy Code.

6. The Disclosure Statement Order further (a) approved the forms of ballots to be used in soliciting votes on and elections under the Plan (collectively, the "Ballots"), (b) established certain balloting procedures to be applied in determining votes on and elections under the Plan, (c) approved the appointment of Lain, Faulkner & Co., P.C. (the "Balloting Agent") as the party responsible for receiving executed Ballots, determining and tabulating votes on and elections under the Plan, and determining whether each particular impaired class of claims under the Plan has accepted or rejected the Plan, subject to final determination by the Court, (d) established a deadline of March 19, 2004 for the return of Ballots to the Balloting

Agent, and (e) established a deadline of March 19, 2004 for the filing and service of objections to confirmation of the Plan (the "Objection Deadline").

7. The Disclosure Statement Order also approved the form and manner of providing notice of the Confirmation Hearing and of the Objection Deadline, establishing a deadline of February 6, 2004 for the mailing of solicitation materials to creditors and other parties in interest. As evidenced by Proponents' Exh. 5, the Proponents timely complied with such requirement. Accordingly, adequate and sufficient notice of the Confirmation Hearing and Objection Deadline has been provided to creditors and other parties in interest, and the Proponents properly and fairly distributed Ballots and all of the other solicitation materials referenced above to the holders of claims who were entitled to vote on and make elections under the Plan.

8. On March 19, 2004, certain medical providers (collectively, the "Objecting Providers") filed their Various Providers' Consolidated Objections to the Confirmation of Proponents' First Amended Joint Liquidating Plan (the "Objection").

9. On April 14, 2004, the Proponents filed an Amended Joint Motion to Extend and/or Modify Voting Deadline (the "Ballot Extension Motion"), whereby the Proponents requested that certain untimely Ballots be treated as timely and counted for all purposes except for determining acceptance or rejection of the Plan. On April 21, 2004, prior to the commencement of the Confirmation Hearing, the Court granted the Ballot Extension Motion. On April 30, 2004, the Court entered an order reflecting same (the "Ballot Extension Order"), which also identifies the claimants determined to have timely made the election to opt in to the Third-Party Settlement under the Plan (collectively, the "Additional Opt In Claimants") and the claimants determined to have timely made the election to have their claims treated as Class 5 Convenience Claims under the Plan (collectively, the "Additional Class 5 Electing Claimants").

10. On April 20, 2004, the Committee filed a Supplement to the Ballot Extension Motion (the "Ballot Extension Motion Supplement"), whereby the Committee, on behalf and at the request of certain claimants who timely made the election to opt in to the Third-Party Settlement under the Plan (collectively, the "Supplemental Opt In Claimants"), requested the Court to enter an order authorizing the Supplemental Opt In Claimants to revoke their Class 5 Convenience Claim elections. On April 29, 2004, the Court entered an order granting the Ballot Extension Motion Supplement (the "Ballot Extension Supplement Order"), which also identifies each of the Supplemental Opt In Claimants.

11. On April 17, 2004, the Proponents filed an Expedited Motion for Approval of Compromise with Certain Providers (the "Compromise Motion"), whereby the Proponents requested approval of a settlement reached by the Trustee with the Objecting Providers in resolution of a number of contested matters in the Bankruptcy Case, including the Objection. On April 21, 2004, prior to the commencement of the Confirmation Hearing, the Court granted the Compromise Motion and on the same date entered an order reflecting same (the "Compromise Order"). Pursuant to the settlement and Compromise Order, (a) each of the Claims held by the Non-Electing Providers (as defined in the Compromise Order) were withdrawn, thereby also resulting in each of the Non-Electing Providers' votes on the Plan being withdrawn pursuant to Fed. R. Bankr. P. 3006, and (b) the Objection was withdrawn. No other objections to confirmation of the Plan have been filed.

12. On May 5, 2004, during the course of the continued Confirmation Hearing, the Proponents agreed to make certain modifications to the Plan to address certain isolated concerns raised by the Court during such hearing. Accordingly, on May 10, 2004, the Proponents filed the Modified Plan, which incorporates such modifications. Because the modifications are non-

material and have no adverse impact on any creditors or other parties in interest in the case, in reference to Section 1127 of the Bankruptcy Code: (a) the Proponents are hereby deemed to have complied with all of the requirements of Section 1125 of the Bankruptcy Code in relation to the Modified Plan; (b) all votes and elections timely and properly cast in relation to the Plan (excluding, however, the votes cast on the Plan which have been withdrawn as a result of the Compromise Order) are deemed to have been timely and properly cast in relation to the Modified Plan; (c) the Ballot Extension Order and the Ballot Extension Supplement Order, insofar as they provide for certain untimely Ballots to be counted, and for certain plan elections to be changed, shall be equally applicable to the Modified Plan; and (d) no time is fixed for creditors to be given the opportunity to change their votes or elections in relation to the Modified Plan because no such opportunity is necessary or warranted given the fact that the modifications to the Plan reflected in the Modified Plan are non-material and have no adverse impact on any of the creditors in this case.

B. Background of the Debtor

13. The Debtor, originally named Harris Methodist Select, was incorporated under the laws of the State of Texas in February 1993. In February 1999, the Debtor changed its name to Medical Select Management. The Debtor is a non-profit corporation under Texas law and has no shareholders.

14. When operational, the Debtor conducted business in the healthcare field as an independent physician association (IPA) certified by the Texas State Board of Medical Examiners under the former provisions of Section 5.01(a) of the Texas Medical Practices Act (later codified as Section 162.001 of the Texas Occupations Code). As a Section 5.01(a) entity, the Debtor was authorized to enter into agreements with the purchasers of healthcare services

and, in fact, entered into a number of agreements with health maintenance organizations (HMOs) and preferred provider organizations (PPOs). The Debtor was also licensed by the Texas Department of Insurance to serve as a third party administrator and utilization review agent.

15. As of the Petition Date, the Debtor had existing contracts with each of the Settling HMOs. *See* Proponents' Exhs. 11 & 12. Pursuant to such contracts, the Debtor agreed to provide or arrange for the provision of medical services to enrollees of the Settling HMOs' health plans, and to be responsible for certain functions such as the processing and payment of claims, utilization review, and credentialing.

16. In order to be in a position to adequately service the medical needs of the enrollees, the Debtor separately contracted with numerous providers in and around Tarrant County, Texas in an effort to establish a sufficiently diverse and widespread network of providers to offer to the enrollees. As of July 2001, the Debtor had reportedly established a network of over 1,700 providers, and by and through its contracts with the providers and the Settling HMOs, the Debtor reportedly serviced the medical needs of roughly 200,000 health plan enrollees.

17. As part of the Debtor's contracts with the Settling HMOs, the Debtor also agreed to be responsible for the payment of certain covered medical services for enrollees assigned to the Debtor. In exchange for same, the Settling HMOs paid the Debtor a monthly payment, calculated on a fixed fee basis in relation to the number of enrollees assigned to the Debtor during the particular month. Significantly, pursuant to such contracts, the Debtor received this "capitated" payment even if the covered medical claims during a particular month were less than or exceeded the amount of the payment. *See, e.g.*, Proponents' Exh. 11 (¶¶ 1.4, 2.1, 5.1, 5.12, 5.13); Proponents' Exh. 12 (¶ 5[A], Attach. A [¶ I(A)(4)-(5)])

18. In relation to the Debtor's contracts with providers, the Debtor correspondingly agreed to pay the providers for those covered medical charges incurred in treating the enrollees assigned to the Debtor under the HMO agreements, and the providers agreed to certain capitated and fixed fee rates on their services.

19. Operationally, prior to January 1, 1999, the Debtor was affiliated with the Harris Methodist Health System ("HMHS"), which served as the Debtor's corporate member. Effective as of January 1, 1999, however, the Debtor's ties with HMHS were severed and the Debtor eliminated HMHS as its member. In January 1999, following the separation, the Debtor contracted with Medical Pathways Management Corporation ("MPMC") to provide the Debtor the operational support that had previously been provided by and through the Debtor's affiliation with HMHS. Pursuant to the Debtor's contract with MPMC, the Debtor agreed to pay MPMC on a basis similar to how the Debtor was being paid by the Settling HMOs (*i.e.* a fixed rate based upon the number of enrollees assigned to the Debtor's provider network in any particular month), and MPMC agreed to process medical claims, manage the payment of covered medical claims for which the Debtor was responsible, manage the Debtor's financial holdings and investments, and manage certain other aspects of the Debtor's operations related thereto. *See* Proponents' Exh. 13.

C. Events Leading to Chapter 11 Filing

20. Prior to the Petition Date, the Debtor's primary source of revenue came from its contracts with the Settling HMOs. The Debtor experienced various problems with its business causing significant losses and ultimately a liquidity crisis leading up to the Petition Date.

21. On July 2, 2001, the Texas Department of Insurance placed the Debtor under supervision, and Neal W. Rockhold (the "TDI Supervisor") was appointed to supervise the

Debtor's operations. Once under supervision, the Debtor, MPMC, the Settling HMOs and the TDI Supervisor engaged in negotiations in an effort to address the Debtor's continuing liquidity problems and looming failure. While certain progress was reportedly made in such negotiations, the Debtor's management determined it necessary to place the Debtor under the protection of bankruptcy and on July 24, 2001, the Debtor filed its voluntary petition for relief under Chapter 11 of the Bankruptcy Code, thereby initiating the Bankruptcy Case.

D. Post-Petition Cessation of Operations

22. Not long after the filing, numerous of the providers, and eventually the Settling HMOs as well, filed motions in the Bankruptcy Case to compel the Debtor's immediate assumption or rejection of their contracts. Shortly before the Trustee's appointment as Chapter 11 trustee, the Court entered orders in the Bankruptcy Case providing for the rejection of the Debtor's contracts with the Settling HMOs, MPMC and numerous of the providers, and the Debtor shortly thereafter ceased operating as a going concern. *See* Proponents' Exhs. 15-17.

E. The Modified Plan's Structure and Treatment of Classes and Claims

23. The Modified Plan provides for the classification of the following categories of claims against the Debtor:

<u>Unclassified Claims</u>
Allowed Administrative Claims
Allowed Priority Tax Claims

<u>Classified Claims</u>
Class 1: Allowed Secured Claim of BOA
Class 2: Allowed Secured Claim of PacifiCare
Class 3: Other Allowed Secured Claims
Class 4: Allowed Priority Non-Tax Claims
Class 5: Allowed Convenience Claims
Class 6: Allowed Tort Claims
Class 7: Allowed General Unsecured Claims
Class 8: Allowed Voluntarily Subordinated Claims
Class 9: Allowed Involuntarily Subordinated Claims

Article 2 of the Modified Plan clearly identifies each of these classes of claims, and the particular types of claims encompassed within each such class are adequately described in reference to the definitions set forth in Article 1 of the Modified Plan. Sections 4.1.5, 4.2.3, 4.3.3, 4.4.2, 4.5.3, 4.6.3, 4.7.5, 4.8.6 and 4.9.2 of the Modified Plan, respectively, identify whether each such class is impaired or unimpaired under the Modified Plan. Classes 1-5 are designated as unimpaired under the Modified Plan, and Classes 6-9 are designated as impaired under the Modified Plan. Such designations are proper and supported by the provisions of Section 1124 of the Bankruptcy Code and applicable law.

24. Except for the class of Allowed Convenience Claims (Class 5), the claims placed within each class of the Modified Plan are substantially similar to the other claims in each such class, and there are substantial differences in the legal nature and/or priority of the claims of each class from the claims in each other class. Class 5 (consisting of Allowed Unsecured Claims of $500.00 or less) was established by the Proponents for administrative convenience. The parameters set for Class 5 are reasonable and necessary to avoid the complications associated with factoring *de minimus* claims into the pro rata distribution scheme established for Class 7 Claims.

25. Article 4, in conjunction with Articles 6-10, 12 and 13 of the Modified Plan, detail how the Modified Plan proposes to treat each class of claims under the Modified Plan. All claims contained within each particular class will receive the same treatment under the Modified Plan, unless the holder of a particular claim within such class agrees to a less favorable treatment of its claim.

26. The Modified Plan also provides for certain voluntary elections to be made as to treatment under the Modified Plan. In particular, each holder of a Class 7 claim was given the

opportunity, by and through the balloting process, to (a) opt in to the Third-Party Settlement offered under the Modified Plan (resulting in a bifurcation of Class 7 into Class 7-A, Allowed Opt-In Claims, and Class 7-B, Allowed Opt-Out Claims, for purposes of distributions), and (b) reduce its claim to $500.00 and have the claim treated as a Class 5 Convenience Claim. Additionally, Class 8 (Allowed Voluntarily Subordinated Claims) includes procedures for the determination of both the amount and the priority of such claims, albeit on a subordinated basis, at a later date (*i.e.* if and when funds become available for distribution to Class 8) and, therefore, is also bifurcated into two classes for distribution purposes: Class 8-A, Allowed Administrative Subordinated Claims; and Class 8-B, Allowed Non-Administrative Subordinated Claims. All claims contained within each of the above-described bifurcated classes will also receive the same treatment under the Modified Plan, unless the holder of a particular claim within such class agrees to a less favorable treatment of its claim.

27. Articles 6, 7, 9, 10, 12 and 13 of the Modified Plan specify in detail how the Modified Plan will be implemented. Among other things: (a) Section 6.1 of the Modified Plan provides for the establishment, funding and administration of the Creditor Trust, and for the appointment of the Creditor Trust Trustee, the Creditor Trust Advisory Committee, and their respective successors; (b) Section 6.2 of the Modified Plan provides for the post-confirmation management and eventual dissolution of the Debtor; (c) Section 6.3, Article 7 and Article 13 of the Modified Plan provide for the consummation of the settlements proposed by and through the Modified Plan; and (d) Articles 9 and 10 of the Modified Plan detail how Disputed Claims will be resolved and the mechanics for distributions under the Modified Plan.

28. Section 3.1.2 of the Modified Plan provides that any payments made or to be made for services or for costs and expenses in or in connection with the Bankruptcy Case are

subject to the approval of the Court as reasonable. Section 6.1.10 sets out the provisions applicable to the payment of fees and costs and expenses incurred in administering the Creditor Trust, which payments are subject to the oversight of the Creditor Trust Advisory Committee pursuant to the provisions of Section 6.1.13 of the Modified Plan. The compensation and reimbursement provisions set out in Section 6.1.10 of the Modified Plan are reasonable.

29. Except to the extent that the holder of a particular claim of the type described below agrees to a different treatment of such claim: (a) claims of a kind specified in Section 507(a)(1) of the Bankruptcy Code will be paid in full in cash equal to the allowed amount of such claims pursuant to the provisions of Section 3.1 of the Modified Plan; (b) claims of a kind specified in Sections 507(a)(3), (a)(4) and (a)(6) of the Bankruptcy Code will be paid in full in cash equal to the allowed amount of such claims pursuant to the provisions of Section 4.4.1 of the Modified Plan; and (c) claims of a kind specified in Section 507(a)(8) of the Bankruptcy Code will be paid in full in cash equal to the allowed amount of such claims pursuant to the provisions of Section 3.2.1 of the Modified Plan. There are no claims in the Bankruptcy Case of a kind specified in Sections 507(a)(2), (a)(5) or (a)(7) of the Bankruptcy Code.

30. The Modified Plan provides for the liquidation of the Debtor. Based upon the resources that will be made available to the Creditor Trust on the Effective Date of the Modified Plan, in particular the settlement payments to be made by the Settling Parties (which must be received by the Creditor Trust in order for the Modified Plan to become effective), the Creditor Trust will have sufficient cash to make all payments required by, and on the timeframes established under, the Modified Plan, and confirmation of the Modified Plan is not likely to be followed by the need for any additional financial restructuring or liquidation.

31. Pursuant to the provisions of Section 3.1 of the Modified Plan, all fees payable under Section 1930 of Title 28 of the United States Code which are assessed prior to the Effective Date of the Modified Plan and remain unpaid as of the Effective Date will be paid promptly following the Effective Date of the Modified Plan, and any such fees assessed from and after the Effective Date will be paid by the Creditor Trust as they come due.

32. Article 8 of the Modified Plan sets out the provisions for the assumption or rejection of all of the Debtor's remaining executory contracts and unexpired leases under Section 365 of the Bankruptcy Code. On March 19, 2004, in accordance with the provisions of Section 8.2 of the Modified Plan, the Trustee filed his Notice Pursuant to Section 8.2 of Proponents' First Amended Joint Liquidating Plan (the "365 Notice"), whereby the Trustee identified several insurance policies and related agreements (collectively, the "Insurance Agreements") as contracts to be assumed as of the Effective Date of the Modified Plan. The 365 Notice, along with a copy of the Disclosure Statement, was served on each of the counter-parties to the Insurance Agreements. *See* Proponents' Exh. 6. No objections to the 365 Notice or to confirmation of the Plan (which would be applicable to the Modified Plan as well) have been timely asserted by any of the counter-parties to the Insurance Agreements. No defaults exist under the Insurance Agreements and no cure payments are required under Section 365(b) of the Bankruptcy Code. The Creditor Trust, as the transferee of the Insurance Agreements and of all of the rights thereunder, will be capable of performing all future obligations under the agreements following the Effective Date of the Modified Plan. Accordingly, the Trustee's assumption of the Insurance Agreements is warranted and in the best interest of the estate and creditors.

33. The Debtor does not charge any rates that are subject to approval by a governmental regulatory commission. Similarly, the Debtor does not have a retirement program, and therefore there are no retiree benefits subject to continuation after the Effective Date of the Modified Plan.

F. Settlements Under the Modified Plan

34. The Modified Plan is premised on the consummation of an overall settlement reached between the Proponents, on the one hand, and the Pathways Parties[2] and Settling HMOs (collectively, the "Settling Parties"), on the other hand. Pursuant to the overall settlement, the Settling Parties will collectively pay at least $7,470,000.00 to the Creditor Trust established under the Modified Plan, and the Settling Parties' unsecured claims in the case will be subordinated. Article 7 of the Modified Plan sets out in detail the terms and conditions of this overall settlement, which can effectively be broken down into three (3) component settlements, each of which is integral and dependent upon the others:

(a) The Estate Settlement. Part of the overall settlement is focused on the resolution of claims held by the estate against the Settling Parties and by the Settling Parties against the estate (the "Estate Settlement"). By and through the Estate Settlement, $2.0 million of the settlement proceeds to be paid by the Settling Parties to the Creditor Trust will constitute General Trust Assets (available for any use consistent with the Modified Plan), and each of the Settling Parties' unsecured claims in the case, which aggregate in excess of $40.0 million (*see* Proponents' Exhs. 18-21), will be subordinated, resulting in no payments being made on such claims under the Modified Plan unless and until each and every Allowed General Unsecured Claim under the Modified Plan has been paid in full. In exchange for same, the Settling Parties will be released from any and all liability to the estate (with certain exceptions including the estate's restitution award against Frederick C. Miller ["Miller"], one of the Pathways Parties [*see* Proponents' Exh. 25]), and both the estate and the Settling Parties will be deemed to have released the Debtor's board of directors (the "Board") and certain advisory committee

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[2] The Pathways Parties consist of MPMC, Medical Pathways Management – Texas, Inc. ("MPMT," an affiliate of MPMC to whom MPMC assigned its contract with the Debtor; MPMT and MPMC collectively referred to as "Pathways") and certain past and present officers of Pathways (Michael J. Eberhard, Edward Rotan and Frederick C. Miller).

members to the Board (the Board and such committee members are collectively referred to as the Debtor Parties under the Modified Plan).[3]

(b) The Third-Party Settlement. Another part of the overall settlement is focused on the resolution of claims held by providers and other unsecured creditors against the Settling Parties (the "Third-Party Settlement"). By and through the Third-Party Settlement, the specific terms and conditions of which are set out in Section 7.5 of the Modified Plan, the remaining settlement proceeds to be paid by the Settling Parties to the Creditor Trust ($5,470,000.00, with the potential for such amount to increase by as much as $350,000.00 based upon the total allowable provider claims in the case and the terms of the PacifiCare settlement) will constitute Earmarked Trust Assets distributable solely to those creditors who have elected to participate in the settlement. Each holder of a General Unsecured Claim who elected (using its Ballot) to opt in to the settlement will be entitled to a pro rata share of the Earmarked Trust Assets. By making the election, the holder has agreed, and will be deemed bound on the Effective Date of the Modified Plan, to the release, waiver and injunction provisions set forth in Sections 7.5.3, 7.5.4, 7.5.5, 13.1, 13.6 and 13.7 of the Modified Plan. Of note, while the Third-Party Settlement is an essential component of the overall settlement reached with the Settling Parties, participation in the settlement is completely voluntary. Only those creditors who affirmatively elected to opt in to the Third-Party Settlement (by checking the appropriate box on the Ballot) will be bound by the terms of the Third-Party Settlement.

(c) The Avoidance Action Settlement. The final component of the overall settlement relates to the estate's avoidance action claims against creditors (the "Avoidance Action Settlement"). By and through the Avoidance Action Settlement, the terms and conditions of which are set forth in Section 7.5.2(b) of the Modified Plan, those creditors holding General Unsecured Claims who have both voted to accept the Modified Plan and elected to opt in to the Third-Party Settlement will be released from avoidance action liability to the estate on the Effective Date of the Modified Plan.

35. In agreeing to the overall settlement, the Proponents considered the following factors: (a) the likelihood of success in litigation; (b) the complexity and duration of such litigation, and the attendant expense, inconvenience and delay that would result; and (c) creditor support for the overall settlement. To put these factors into context, it is first important to consider the events which led to the Proponents' settlement with the Settling Parties.

[3] The release of the Debtor Parties excludes, however, any and all defenses and objections that the Debtor, Debtor's estate, the Trustee, the Creditor Trust, or the Creditor Trust Trustee hold or may hereafter hold in relation to Claims, if any, asserted by the Debtor Parties in the Bankruptcy Case and the estate's restitution award against Miller.

The Trustee's Investigation and Initiation of Litigation, and the Negotiations Thereafter

36. Other than certain cash, investments, and office equipment of nominal value, the Debtor had virtually no tangible assets of significant value when the Trustee first became involved in the Bankruptcy Case. The Debtor's primary assets were intangible contract rights and causes of action. Against this backdrop, the Debtor had scheduled liabilities of nearly $45.0 million, and by December 4, 2001 (the deadline for filing claims in the case), there were over $100.0 million in claims asserted in the case. Hence, the Trustee quickly came to believe that if creditors were to obtain any meaningful recovery in the case, it would be through the pursuit of the Debtor's causes of action.

37. Over the course of several months following the Trustee's appointment, and with the assistance of his professionals, the Trustee conducted an extensive investigation into the cause of the Debtor's dramatic financial downfall. The focus of the Trustee's investigation was on the various actions and omissions taken by each of the parties having a significant managerial or contractual role in the Debtor's operations. The Trustee met with and collected information and documents from numerous providers and/or their counsel, the Debtor's prior management, the Debtor's attorneys, Pathways' representatives and their counsel, the Settling HMOs and their counsel, representatives of the Texas Attorney General's Office and Texas Department of Insurance, members of the Committee and Committee counsel, the Debtor's lender's counsel, and agents of the Federal Bureau of Investigation (who had opened an investigation into certain actions taken by Miller, the Debtor's prior Treasurer and a prior officer of Pathways).

38. Utilizing the input and information obtained through such investigation, along with the information obtained from review of the Debtor's books and records and other available financial data and information, the Trustee sought to reconstruct the genesis of the Debtor's

financial crisis and determine the reasons for the Debtor's failure to stem, and/or otherwise rectify, its problems in a timely fashion. It was also important to the Trustee to obtain an understanding of the nature and magnitude of allowable claims in the case. The bulk of the allowable unsecured claims in the case are held by medical providers who were not paid over the course of several months leading up to the Petition Date. In fact, of the $16.2 million in allowable General Unsecured Claims estimated by the Trustee, the estimated amount attributable to non-provider claimants is less than $450,000.00.

39. Ultimately, the Trustee came to believe that there was not a single party exclusively responsible for the Debtor's demise. Instead, he believed it likely that each of the parties involved in, or having some degree of oversight over, the Debtor's operations had some level of responsibility in the downfall. The Trustee's determination of who to initially proceed against in litigation was largely dictated by the Trustee's perception of relative responsibility as between the parties, and the legal and contractual ramifications and limitations of the actions and omissions taken by the parties.

40. On November 30, 2001, the Trustee commenced a lawsuit against the Pathways Parties (the "Pathways Lawsuit"), asserting claims of breach of fiduciary duty, gross negligence, negligent misrepresentation and breach of contract. In response to the complaint, Pathways and certain of the other Pathways Parties asserted counterclaims against the Debtor's estate, third-party claims against PacifiCare and certain of its affiliates, third-party claims against certain members of the Board, and a number of responsible party designations under Chapter 33 of the Texas Civil Practice and Remedies Code. Thus, as a practical matter, the Pathways Lawsuit served as the catalyst to bring substantially all of the key parties together into a single dispute forum.

41. In light of same, and given the sheer number of parties involved in the litigation, with the consent of each of the major parties the Trustee requested that a global mediation take place. The Court agreed and a mediation was scheduled shortly thereafter, in which the Committee and Aetna also agreed to participate. The Honorable Harlin D. Hale, a practicing attorney at the time (who was appointed as a federal bankruptcy judge for the Northern District of Texas prior to the final mediation session between the parties), was appointed to serve as the mediator. Leading up to the mediation, the parties also engaged in extensive document discovery and virtually tens of thousands of pages of documents were exchanged and reviewed.

42. Over a period of several months, the Proponents and Settling Parties attended three separate mediation sessions, and engaged in protracted, often contentious, negotiations with each other. Two factors served to frame the ultimate settlement reached in the case: first, given the tangled web of contractual and legal relationships between the Debtor and Pathways, the Settling HMOs, the providers, and the Board, it became clear to the Trustee that isolated litigation and negotiations would be both impractical and unrealistic; second, Pathways and PacifiCare conditioned any settlement with them on the resolution of claims held by the providers and other unsecured creditors against them as well.

43. Ultimately, a settlement between the parties was reached, a formal term sheet was executed by the parties, and the settlement was memorialized within the Modified Plan. Based upon the foregoing and other proceedings which have taken place before the Court, it is clear to the Court that the settlement was the product of extensive, good faith, arm's length negotiations between the Proponents and Settling Parties.

Likelihood of Success in Litigation

44. Focusing on the likelihood of success on the various claims asserted, or which could be asserted, the Trustee provides the following insight:

(a) Claims Relating to Pathways. The Trustee believes that there is a strong likelihood that he would be successful in litigation against Pathways if the litigation were to proceed. However, the Trustee further notes that there exists a degree of uncertainty as to the net recovery to be achieved by the estate in such litigation. In particular, three factors presented concern to the Trustee: (i) Pathways' rejection damage claim (in excess of $13.8 million), to the extent allowed, could serve, in whole or in part, as an offset against any judgment obtained against Pathways; (ii) Pathways' responsible third-party allegations under Texas' comparative fault provisions (whereby Pathways has alleged that the Debtor's Board, the Settling HMOs, and certain additional parties share responsibility in the Debtor's downfall), to the extent successful, could effectively minimize the damages assessed against Pathways; and (iii) Pathways' third-party claims against the Board and PacifiCare, to the extent successful, could result in additional liability to the estate (by creating/increasing their claims against the estate). The Trustee believes that there is significant risk that any result obtained through litigation will not be comparable to the settlement currently proposed (whereby Pathways' $13.8 million claim will be subordinated, the Creditor Trust will receive $2.0 million in settlement of the estate's claims, and the Creditor Trust will receive an additional $3.65 million in earmarked funds for the benefit of creditors who elected to opt in to the Third-Party Settlement under the Modified Plan).

(b) Claims Relating to the Settling HMOs. The Trustee believes that the likelihood of success in litigation against the Settling HMOs is more difficult to predict. First, because the Debtor entered into capitation agreements with the Settling HMOs, whereby the Debtor contractually obtained the upside benefit of the capitation exceeding the health care costs and the corresponding risk that the funding provided would not be sufficient to satisfy provider claims, the Settling HMOs have asserted that the Debtor has no recourse against them. The Trustee recognizes that the estate faces risk on this argument. Second, in relation to the funding provided by Aetna, the Trustee believes that certain of the Aetna capitation funds (as much as several million dollars) were likely used by the Debtor to pay for provider charges incurred in rendering services to PacifiCare health plan enrollees (instead of Aetna health plan enrollees), thereby placing into doubt whether and/or to what extent the Debtor was under-funded by Aetna. Third, while the Trustee believes that both of the Settling HMOs may have had a duty to timely address the Debtor's problems as a result of their oversight obligations under Texas law, based upon his investigation, the Trustee also believes that the financial reports generated by Pathways for the Debtor during the relevant time period were inaccurate and failed to reflect the magnitude of the losses being sustained by the Debtor. The Settling HMOs deny that they had a duty to take any action in relation to the Debtor's problems and also raise the inaccurate financial reporting as a defense. The Settling HMOs have also asserted a myriad of other defenses – these include that the Trustee does not have standing to claim that the Debtor was not properly supervised, that the Debtor was damaged by its own conduct, and that the Debtor engaged in faulty utilization and other actions that caused its losses. Additionally, the Trustee notes that Miller, a prior officer of the Debtor and Pathways, likely forged certain documents in an apparent effort to mislead PacifiCare. In relation to same, PacifiCare has asserted certain monetary counterclaims against the estate (including fraud-based claims), which also present significant risk to the estate. Finally, the Trustee explains that the Settling HMOs' rejection damage claims in the Bankruptcy Case, which total in excess of $26.6 million in the aggregate, could serve as an offset against any judgment obtained against the Settling HMOs, to the extent such claims are allowed. The Trustee believes that there is significant risk that any result obtained through litigation will not be comparable to the settlement currently proposed (whereby $26.6 million in claims held by the Settling HMOs will be subordinated and the Creditor Trust will receive at least $1.82 million in earmarked funds for the benefit of creditors who elected to opt in to the Third-Party Settlement under the Modified Plan).

(c) Claims Against Board. As part of the settlement with the Settling Parties, the estate's claims against the Board will be released. If, instead, such claims were to be pursued, the Trustee believes that there is some likelihood that the litigation would be successful. However, the Trustee anticipates that the Board would assert that they were also misled by Pathways, which presents risk. The Trustee further explains that the pursuit of litigation against the Board is, at least to some degree, contradictory to the pursuit of litigation against Pathways because it results in the shifting of blame for the Debtor's failure. Finally, the Trustee considered the risk of certain other defenses potentially available to the Board, such as the business judgment rule and certain protections provided by the Debtor's bylaws. The Trustee believes that the settlements reached with the Settling Parties outweigh any benefit to be obtained by pursuing litigation against the Board.

(d) Claims Against Creditors on Avoidance Action Claims. Finally, in relation to avoidance action claims held by the estate against creditors, in particular preference claims, the Trustee believes that there is a strong likelihood of success in such litigation, with the amount recoverable much less certain. The Trustee anticipates that the claimants would assert certain statutory defenses in an effort to minimize their exposure on such claims, some or all of which defenses may have some likelihood of success at some level. The Trustee also notes that avoidance litigation, alone, will only result in a reallocation of the recoveries among creditors, with no net benefit to the estate. The settlements obtained with the Settling Parties, on the other hand, will result in a net benefit to the estate and creditors. Given that the settlement is conditioned on confirmation of the Modified Plan, and confirmation of the Modified Plan is conditioned on a sufficient level of participation by creditors in the Third-Party Settlement offered under the Modified Plan, and taking into account the fact that those who opt in to the Third-Party Settlement will be giving up their right to pursue the Settling HMOs on claims that they may have against them in the face of avoidance litigation, the Trustee believes that the benefits to be obtained through releasing

> those creditors who accept the Modified Plan and elect to opt in to the Third-Party Settlement (so as to enable confirmation of the Modified Plan) outweigh the retention of avoidance action claims against such creditors and any potential for recovery on such claims.

The Trustee's reasoning and analysis is well-founded and compelling, and supports approval of each of the individual settlements embodied within the Modified Plan.

Complexity and Duration of Litigation, and Attendant Expense, Inconvenience and Delay

45. Equally compelling is the likely complexity and duration of such litigation (focusing predominantly on the litigation against Pathways, the Settling HMOs and the Board), and the attendant expense, inconvenience and delay that would result. The Trustee explains that, gauged upon the sheer number of documents that were exchanged by the parties in advance of the mediation, and given the tangled web of contractual and legal relationships at stake, the litigation would not only be complicated, but also extremely protracted and time consuming. He further explains that a successful outcome in such litigation would likely be followed by appeals, which could result in additional years of delay in reaching final conclusion to the Bankruptcy Case. Of great concern to the Trustee is the cost of litigation. There are minimal estate resources available to fund such litigation. *See* Proponents' Exh. 26 (February 2004 Monthly Operating Report). Hence, the Trustee believes that the expenses of such litigation would have to be funded on a contingent fee arrangement, which customarily provides for 33.3% (and up to 40.0% in the event of an appeal) of the gross recovery to be paid as the fee for legal services, with all out-of-pocket expenses to be paid from the net proceeds thereafter. Thus, the Trustee believes that these factors, as well, support approval of the settlements set forth in the Modified Plan. The Court agrees.

Other Factors/Creditor Support for the Settlements

46. Finally, and perhaps most compelling, is the creditor support for the settlements. The Committee, which represents the interests of all unsecured creditors, supports approval of the settlements and is a co-proponent of the Modified Plan. More significantly, the unsecured creditors themselves overwhelmingly support the settlements, as evidenced by the voting outcome on the Modified Plan.[4] As set out in greater detail below, of the holders of General Unsecured Claims who timely voted on the Modified Plan, over 98% of them (holding in excess of $14,852,911.00 in allowable claims for voting purposes) voted to accept the Modified Plan. Similarly, over 98% of the holders of General Unsecured Claims who timely voted on the Modified Plan also elected to opt in to the Third-Party Settlement under the Modified Plan. Both of these additional factors weigh in favor of approving the settlements.

47. For all of the foregoing reasons, the Court finds that the settlements set forth in the Modified Plan were entered into in good faith, and that they are fair, equitable, reasonable, supported, and in the best interests of both the estate and creditors, and should therefore be approved.

G. Voting Results

48. The only impaired classes of claims under the Modified Plan are Classes 6-9. Hence, only the holders of claims within such classes were entitled to vote on the Modified Plan. The Proponents timely provided Ballots to each of the holders of claims within Class 7 and Class 8 of the Modified Plan. There are no existing claims in Class 6 and Class 9 under the Modified Plan; therefore, no Ballots were provided and no Ballots were cast in relation to such classes.

[4] As explained in paragraph 12 above, the voting results in relation to the Plan are equally applicable to the Modified Plan.

49. Pursuant to the Disclosure Statement Order, only those properly completed and executed Ballots actually received by the Balloting Agent on or before 5:00 p.m. (Central Time) on March 19, 2004 (the "Voting Deadline") were to be counted in determining votes on and elections under the Plan, absent extension of the Voting Deadline by the Court. Pursuant to the Ballot Extension Order, the Voting Deadline was extended to permit certain untimely Ballots to be counted for all purposes in relation to the Plan except for determining acceptance or rejection of the Plan. Similarly, pursuant to the Ballot Extension Supplement Order, the Supplemental Opt In Claimants were permitted to revoke their Class 5 Convenience Class elections, but their Ballots, as modified, are to be counted for all purposes in relation to the Plan (including the election to opt in to the Third-Party Settlement) except for determining acceptance or rejection of the Plan. For the reasons set out in paragraph 12 above, the Voting Deadline, the Ballot Extension Order, the Ballot Extension Supplement Order, and all votes and elections in relation to the Plan (as they are impacted by same) are equally applicable to the Modified Plan.

50. As evidenced by Proponents' Exhibit 31, both Class 7 and Class 8 voted in the requisite numbers and amounts, in reference to Section 1126(c) of the Bankruptcy Code, to accept the Modified Plan.

51. Although the Objection has been withdrawn, one point within the Objection bears comment. The Objecting Providers had asserted that the Class 7 Ballots cast by PacifiCare (on account of certain Class 7 claims assigned to PacifiCare) should not have been counted in determining whether Class 7 had accepted or rejected the Plan (and, hence, the Modified Plan) on the basis that PacifiCare is either an "insider" of the Debtor or, alternatively, on the theory that PacifiCare acquired the Class 7 claims in an effort to control the vote of Class 7.[5] In relation to the allegation that PacifiCare is an "insider" of the Debtor, the evidence clearly demonstrates

[5] The Objecting Creditors also made reference to Aetna, but Aetna did not cast any Ballots in Class 7.

otherwise based upon the lengthy negotiations which took place between the Proponents and PacifiCare in relation to the settlements underpinning the Modified Plan. In any event, there is no evidence supporting the contention that PacifiCare is an "insider" for purposes of the Bankruptcy Code. In relation to the allegation that PacifiCare acquired Class 7 claims in order to control the vote of Class 7, irrespective of the motives of PacifiCare in acquiring the claims, PacifiCare did not obtain a controlling block of votes within Class 7. *See* Proponents' Exhs. 10 & 31. Therefore, there is no compelling reason to disregard the votes cast by PacifiCare in Class 7. In fact, even if the PacifiCare Class 7 Ballots were to be excluded from the count, Class 7 will have still accepted the Modified Plan by over 98% in number and 99% in amount, both percentages clearly within the acceptance thresholds set forth in Section 1126 of the Bankruptcy Code. *See* Proponents' Exhs. 10 & 31.

52. Next, with respect to the elections made by the holders of General Unsecured Claims: (a) Proponents' Exh. 8, the Ballot Extension Order and the Ballot Extension Supplement Order identify (by claimant name) each of the claims for which the holders thereof made the election to opt in to the Third-Party Settlement under the Modified Plan; and (b) Proponents' Exh. 9 (excluding, however, the claims held by the Supplemental Opt In Claimants identified in the Ballot Extension Supplement Order) and the Ballot Extension Order identify (by claimant name) each of the claims as to which the holders thereof made the election to have the claim reduced to $500.00 and treated as a Class 5 Convenience Claim under the Modified Plan.[6]

[6] Pursuant to the Modified Plan, in full and final satisfaction of Class 5 Allowed Convenience Claims, each such Claim will be paid in full in cash. As with other Class 5 Claims, those who have elected Class 5 treatment for their Class 7 Claims shall have no recourse against any of the Aetna Released Parties, the PacifiCare Released Parties or the Pathways Released Parties for any amount of the Claim in excess of $500.00. *See* Modified Plan, §§ 4.5.1, 4.5.2.

H. Treatment of Rejecting Claims and Classes

53. Classes 6 and 9 of the Modified Plan have neither voted to accept or reject the Modified Plan. The reason for same is that there currently exist no claims in such classes. Because neither of these classes have voted to accept the Modified Plan, the Proponents have requested confirmation of the Modified Plan under the provisions of Section 1129(b)(1) of the Bankruptcy Code in relation to such classes.

54. Class 6 consists of Allowed Tort Claims. Pursuant to Section 4.6.1 of the Modified Plan, Allowed Tort Claims are to be first satisfied from any available insurance, with the residual amount of such claims to be treated as either Class 7 or Class 9 claims under the Modified Plan depending upon the nature of the residual amount of the claim. Specifically, the residual amount is subject to treatment as a Class 7 claim (Allowed General Unsecured Claim), except to the extent that it constitutes exemplary or punitive damages, and subject to treatment as a Class 9 claim (Allowed Involuntarily Subordinated Claim) to the extent that it constitutes exemplary or punitive damages. The subordination of exemplary/punitive damages to all other Allowed Unsecured Claims is proper and justified by the claim priority scheme set forth in Section 726(a) of the Bankruptcy Code. Irrespective of whether the residual amount is treated as a Class 7 or a Class 9 claim, in each case no holder of a claim that is junior in priority to such residual Class 7 or Class 9 claim will receive or retain any property under the Modified Plan unless and until such residual Class 7 or Class 9 claim, respectively, is paid in full. The Modified Plan's treatment of Class 6 Allowed Tort Claims is fair and equitable and does not discriminate unfairly.

55. Class 9 consists of Allowed Involuntarily Subordinated Claims. Involuntarily Subordinated Claims are defined in the Modified Plan as claims which are subordinate in

payment to other claims pursuant to, or in accordance with, Section 510 and/or Section 726(a)(4) of the Bankruptcy Code. Pursuant to Section 4.9.1 of the Modified Plan, the holders of such claims will not receive any distributions under the Modified Plan until the allowed claims in each of the classes of claims of higher priority have been paid in full. Such treatment is appropriate and justified based upon the subordination provisions of Sections 510 and 726(a)(4) of the Bankruptcy Code. Accordingly, the Modified Plan's treatment of Class 9 Allowed Involuntarily Subordinated Claims is fair and equitable and does not discriminate unfairly.

56. Shifting to the impaired classes of claims that accepted the Modified Plan, while Class 8 claimants unanimously voted to accept the Modified Plan, certain Class 7 claimants voted to reject the Modified Plan. In relation to such rejecting Class 7 claimants, it is in the best interests of such creditors for the Modified Plan to be approved because such holders will receive distributions under the Modified Plan on account of their claims having a value that is at least equal to the value that they would obtain if the Bankruptcy Case were converted to a Chapter 7 liquidation. First, if a Chapter 7 trustee were to be successful in keeping the settlements proposed by and through the Modified Plan intact in Chapter 7, a result which is unrealistic, the result would be no different in Chapter 7 because the Modified Plan already provides for the Debtor's liquidation (noting, however, that certain additional administrative expenses could actually diminish recoveries in Chapter 7). A more likely scenario, however, would be that the settlements do not remain intact, necessitating the pursuit of litigation by the Chapter 7 trustee. The pursuit of litigation would likely result in a lower return to Class 7 creditors in a Chapter 7 liquidation for the following reasons:

(a) First, in the absence of settlement, over $40.0 million in claims collectively held by Pathways and the Settling HMOs (a portion of which has been asserted as having administrative expense priority) are no longer subordinated to claims within Class 7 under the Modified Plan. Hence, the existence of such claims will significantly dilute recoveries to Class 7 claimants in a Chapter 7 proceeding in the absence of successful litigation to subordinate such claims. For the reasons previously stated in relation to approval of the settlements, there is substantial risk to Class 7 claimants that some or all of the $40.0 million in claims would not be subordinated in a Chapter 7 liquidation (and/or would otherwise serve as an offset against any damages awarded against such parties).

(b) Second, there would be additional administrative costs in a Chapter 7 proceeding. Among other things, the Trustee has indicated that the costs of litigation would have to be funded on a contingent fee basis (with a fee structure of 33.3% to 40.0% of any gross recoveries obtained), which would greatly diminish the net recovery to the estate on any litigation recoveries. Coupled with the subordination issues described above, a Chapter 7 trustee would not only have to succeed on all litigation fronts, but also obtain a substantial recovery in litigation in order to match that which is already available through the settlements, a result which is unlikely in the Court's view.

(c) Third, creditors will lose the benefit of obtaining immediate distributions under the Modified Plan. If litigation is pursued, such litigation could take years to conclude in the event of an appeal, which would likewise result in a significant delay in distributions. This loss in the time-value of money likewise diminishes the value to be achieved in a Chapter 7 liquidation, and in combination with the other factors described above, leads to the conclusion that the value to be obtained by Class 7 creditors under the Modified Plan will exceed the value that they would obtain in a Chapter 7 liquidation.

(d) Finally, conversion to Chapter 7 would result in significant claims administration complications. Among other things, conversion would result in a re-opening of the bar date for asserting claims in the case. During the course of the Chapter 11 proceeding, numerous claims have been disallowed on the basis of their untimely submission; these same claims could be reasserted following conversion of the case. Additionally, while most of the unresolved provider claims in the case have been finally determined pursuant to the Proponents' motion to determine the allowed amount of provider claims for plan purposes, in the event of conversion, the motion is no longer viable and significant expense may be incurred in resolving such claims. These factors are also likely to diminish the return to Class 7 creditors in a Chapter 7 scenario.

I. Other Confirmation Factors

57. The Modified Plan complies with all applicable provisions of the Bankruptcy Code and the Proponents have complied with all applicable provisions of the Bankruptcy Code.

58. Taking into account the nature and amount of the claims scheduled and asserted in the Bankruptcy Case, the Debtor's nominal remaining tangible assets, the causes of action

held by the Debtor/estate against third parties, and the numerous issues affecting the potential for a global resolution of the case (as detailed above), the Proponents clearly formulated and proposed the Modified Plan with the legitimate and honest purpose of effecting a liquidation of the Debtor's remaining assets, with the proceeds thereof to be distributed as expediently and efficiently as possible to the holders of Allowed Claims in the Bankruptcy Case consistent with the priorities established under the Bankruptcy Code. Accordingly, the Proponents have proposed the Modified Plan in good faith and not by any means forbidden by law.

59. Neither the Proponents, nor their respective professionals, solicited acceptances of the Plan (which are equally applicable to the Modified Plan) prior to transmission of the Disclosure Statement to the holders of claims in the Bankruptcy Case. As noted in paragraph 12 above, no solicitation of votes in relation to the Modified Plan is required, nor has any solicitation taken place, because the Modified Plan merely incorporates certain non-material modifications to the Plan which have no adverse impact on any creditors in this case, and all votes cast in relation to the Plan are deemed equally applicable to the Modified Plan.

60. All of the requisite disclosures have been made by the Proponents. In particular:

(a) Section IX(B) of the Disclosure Statement disclosed the identity and affiliation of the individual proposed to serve as the Debtor's sole director and officer following the Effective Date of the Modified Plan, and Section IX(A)(4) of the Disclosure Statement disclosed the identify and affiliation of the individual proposed to serve as the Creditor Trust Trustee following the Effective Date of the Modified Plan. In each case, it is proposed that the Trustee be the person initially appointed to serve in such capacities, which is consistent with the interests of creditors in the Bankruptcy Case and with public policy.

(b) It is not contemplated that any insider of the Debtor will be employed or retained by Debtor following the Effective Date; therefore, no disclosures related to same were necessary.

61. Each of the Settling Parties has approved the form and terms of the Disclosure Statement, Modified Plan, Ballots, solicitation materials and Creditor Trust Documentation.

62. Each of the Settling Parties has approved the adequacy of notice provided to creditors in conjunction with the Plan, the Modified Plan, and the Confirmation Hearing.

63. If and to the extent that each of the conditions to confirmation of the Modified Plan set forth in Section 11.1(c) of the Modified Plan have not been satisfied, PacifiCare has waived such conditions in writing.

64. If and to the extent that each of the conditions to confirmation of the Modified Plan set forth in Section 11.1(d) of the Modified Plan have not been satisfied, Pathways has waived such conditions in writing.

65. Each of the Proponents and Settling Parties have acknowledged that the conditions set forth in Section 11.1(e) of the Modified Plan will be met upon the Court's entry of these findings of fact and conclusions of law and an order confirming the Modified Plan.

66. If and to the extent that the conditions to confirmation of the Modified Plan set forth in Section 11.1(f) of the Modified Plan have not been satisfied, each of the Settling Parties has waived such conditions in writing.

67. Section 11.2(c) of the Modified Plan sets out as a condition to the effectiveness of the Modified Plan that the order confirming the Modified Plan be a Final Order. Pursuant to said section, the condition may be waived. In the event of an appeal from the confirmation order, in the absence of the entry of an order staying such order pending appeal, the Proponents and other parties in interest shall be acting in good faith if they waive the condition and proceed to consummate the Modified Plan and the settlements, transfers and transactions contemplated thereby notwithstanding the appeal, even if they act with knowledge of the appeal.

CONCLUSIONS OF LAW

A. Jurisdiction

68. The Court has jurisdiction over the Bankruptcy Case and this proceeding pursuant to 28 U.S.C. §§ 157 and 1334 and Miscellaneous Rule No. 33 entered by the U.S. District Court for the Northern District of Texas on or about August 3, 1984. The matters subject to determination by the Court in connection with this proceeding constitute core proceedings pursuant to 28 U.S.C. § 157(b)(2). Venue of the Bankruptcy Case and this proceeding in this District is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

B. Classification of Claims; Requisite and Permissible Contents of Modified Plan

69. The classification of claims within the Modified Plan complies with Section 1122 of the Bankruptcy Code. Classes 1-5 of the Modified Plan are unimpaired under the Modified Plan pursuant to the provisions of Section 1124 of the Bankruptcy Code.

70. The Modified Plan sets out all of the designations, specifications and provisions required by Section 1123(a) of the Bankruptcy Code.

71. The Modified Plan also includes provisions for the following, which provisions are permissible and approved pursuant to Section 1123(b) of the Bankruptcy Code:

(a) assumption of the Insurance Agreements as of the Effective Date of the Modified Plan which, for the reasons set forth above, the Court approves as in the best interests of the estate and creditors pursuant to the provisions of Section 365 of the Bankruptcy Code;

(b) rejection of all other executory contracts and unexpired leases as of the Effective Date of the Modified Plan which the Court approves as in the best interests of the estate and creditors pursuant to the provisions of Section 365 of the Bankruptcy Code, given the proposed liquidation of the Debtor under the terms of the Modified Plan;

(c) the settlement of claims by and against the Settling Parties under the terms and conditions of the Estate Settlement described above and the settlement of avoidance action claims under the terms and conditions of the Avoidance Action Settlement described above, each of which settlements the Court approves pursuant to Sections 105(a) and 363 of the Bankruptcy Code and Fed. R. Bankr. P. 9019 as in the best interests of the estate and creditors under the factors described in *Connecticut General Life Ins. Co. v. United Companies Fin. Corp. (In re Foster Mortgage Corp.)*, 68 F.3d 914, 917 (5th Cir. 1995);

(d) the retention and enforcement of causes of action of the Debtor and estate pursuant to the provisions of Section 6.5 of the Modified Plan; and

(e) the voluntary settlement of claims against the Settling Parties by the holders of General Unsecured Claims who have elected to settle such claims under the terms and conditions of the Third-Party Settlement described above, and the issuance of a consensual injunction to enforce the release and waiver provisions of such settlement.

C. Acceptance of Plan by Classes of Claims

72. Classes 1-5 of the Modified Plan, and each of the holders of claims in such classes, have accepted the Modified Plan pursuant to the provisions of Section 1126(f) of the Bankruptcy Code.

73. Classes 7 and 8 of the Modified Plan have accepted the Modified Plan consistent with the provisions of Section 1126(c) of the Bankruptcy Code.

74. As a result of no votes having been cast in relation to Classes 6 and 9 of the Modified Plan, such classes have rejected the Modified Plan consistent with the provisions of Section 1126(c) of the Bankruptcy Code.

D. Confirmation Requirements

75. The Modified Plan complies with all applicable provisions of the Bankruptcy Code, as required by Section 1129(a)(1) of the Bankruptcy Code.

76. The Proponents have complied with all applicable provisions of the Bankruptcy Code, as required by Section 1129(a)(2) of the Bankruptcy Code.

77. The Proponents proposed the Modified Plan in good faith and not by any means forbidden by law, as required by Section 1129(a)(3) of the Bankruptcy Code.

78. All payments subject to approval of the Court pursuant to the provisions Section 1129(a)(4) of the Bankruptcy Code have been approved as reasonable, or will be subject to approval by the Court as reasonable, as required by said section of the Bankruptcy Code.

79. The Proponents have made all requisite disclosures required by Section 1129(a)(5) of the Bankruptcy Code. The Trustee's appointment as the initial Creditor Trust Trustee and as the sole director and President of the Debtor, on the Effective Date of the

Modified Plan, is consistent with the interests of creditors and with public policy, as required by Section 1129(a)(5)(A)(ii) of the Bankruptcy Code.

80. The Debtor does not charge any rates which are subject to approval by a governmental regulatory commission. Therefore, Section 1129(a)(6) of the Bankruptcy Code is inapplicable to this case.

81. With respect to each impaired class of claims under the Modified Plan, each holder of a claim within such class has either accepted the Modified Plan or will receive or retain under the Modified Plan on account of such claim property of a value, as of the Effective Date of the Modified Plan, that is not less than the amount that such holder would so receive or retain if the Debtor were liquidated under Chapter 7 of the Bankruptcy Code, as required by Section 1129(a)(7) of the Bankruptcy Code.

82. With the exception of Classes 6 and 9 under the Modified Plan, each class of claims under the Modified Plan has accepted the Modified Plan or is not impaired under the Modified Plan, as required by Section 1129(a)(8) of the Bankruptcy Code. With respect to Classes 6 and 9 under the Modified Plan, the Modified Plan does not discriminate unfairly against, and is fair and equitable to, such classes, as required by Section 1129(b) of the Bankruptcy Code.

83. The Modified Plan's treatment of claims of a kind specified in Sections 507(a)(1)-(a)(8) of the Bankruptcy Code complies with the provisions of Section 1129(a)(9) of the Bankruptcy Code.

84. At least one impaired class of claims under the Modified Plan has accepted the Modified Plan, determined without including any acceptance of the Modified Plan by any insider, as required by Section 1129(a)(10) of the Bankruptcy Code.

85. As required by Section 1129(a)(11) of the Bankruptcy Code, confirmation of the Modified Plan is not likely to be followed by the need for further financial reorganization or liquidation, except as expressly provided for under the terms of the Modified Plan.

86. The Modified Plan provides for the timely payment of all fees assessed in accordance with the provisions of Section 1930 of Title 28 of the United States Code, as required by Section 1129(a)(12) of the Bankruptcy Code.

87. The Debtor does not have a retirement plan. Therefore, Section 1129(a)(13) of the Bankruptcy Code is inapplicable to this case.

E. Modifications to the Plan

88. The Proponents have complied with Section 1125 of the Bankruptcy Code in relation to the modifications made to the Plan by and through the Modified Plan, as required by Section 1127(c) of the Bankruptcy Code.

89. Pursuant to Section 1127(d) of the Bankruptcy Code: (a) all votes and elections timely and properly cast in relation to the Plan (excluding, however, the votes cast on the Plan which have been withdrawn as a result of the Compromise Order) are deemed to have been timely and properly cast in relation to the Modified Plan; (b) the Ballot Extension Order and the Ballot Extension Supplement Order, insofar as they provide for certain untimely Ballots to be counted, and for certain plan elections to be changed, shall be equally applicable to the Modified Plan; and (c) no time is fixed for creditors to be given the opportunity to change their votes or elections in relation to the Modified Plan because no such opportunity is necessary or warranted given the fact that the modifications to the Plan reflected in the Modified Plan are non-material and have no adverse impact on any of the creditors in this case.

F. Confirmation of the Modified Plan

90. For all of the foregoing reasons, and having met all of the requirements for confirmation, the Modified Plan will be confirmed.

SIGNED this 11 day of May, 2004.

Barbara Houser

BARBARA J. HOUSER
UNITED STATES BANKRUPTCY JUDGE